

*United States Court of Appeals
for the Second Circuit*



**APPELLANT'S
BRIEF**

74-2086

To be argued by
GEORGE A. HAHN

ORIGINAL

In The

United States Court of Appeals

For The Second Circuit

GEORGE FELDMAN, Trustee in Bankruptcy of LEASING
CONSULTANTS INCORPORATED, Bankrupt,

Plaintiff-Appellant.

- against -

NATIONAL BANK OF NORTH AMERICA,

Defendant-Appellee.

BRIEF FOR PLAINTIFF-APPELLANT

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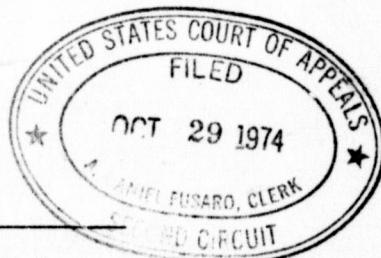


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UNITED STATES COURT OF APPEALS

For the Second Circuit

DOCKET NO. 74-2086

GEORGE FELDMAN, as Trustee in Bankruptcy of Leasing
Consultants Incorporated, Bankrupt,

Plaintiff-Appellant,

against

NATIONAL BANK OF NORTH AMERICA,

Defendant-Appellee.

ON APPEAL from the UNITED STATES DISTRICT COURT

for the EASTERN DISTRICT of NEW YORK

BRIEF FOR PLAINTIFF-APPELLANT

Preliminary Statement

Plaintiff-trustee sought recovery of over \$600,000
from defendant, representing the proceeds of chattel paper
collateral as to which defendant-bank had failed to perfect

2.

its security interest. Defendant moved to dismiss the complaint and plaintiff cross-moved for summary judgment. The motions were heard before District Judge Jack B. Weinstein on June 28, 1974 and the court, in an oral decision (A121-A124), granted summary judgment for defendant on an unpleaded counter-claim and dismissed the complaint. The court then responded to plaintiff's requests for additional findings. (A124-A141) On July 3, 1974, plaintiff filed a motion for reargument (A147-A153) advising the Court that its grant of summary judgment on the unplead counterclaim left plaintiff with a \$167,000 claim against defendant and requesting reconsideration of other issues. The motion was denied on July 8, 1974 (A155) and an "order and judgment" denying plaintiff's motion for summary judgment, granting defendant's motion for summary judgment and dismissing the complaint, was entered the same day. (A156-A157). Plaintiff appeals from that judgment.

Statement of The Case

Defendant-appellee bank made a secured loan to the bankrupt. Security interests in the collateral were granted by two separate instruments. Since the collateral is related to aircraft, perfection of the bank's security interests in the collateral is governed by the Federal Aviation Act of 1958, 49 U.S.C. §1301 et. seq. and Regulations promulgated

thereunder (Chapter 14, Code of Federal Regulations). That statute requires recordation of the security instruments in order to make the security interest valid against third persons without actual notice, i.e., to achieve perfection.

Though the bank tried to record both security instruments, the bank succeeded in recording only one of the two.

The collateral package included all of the bankrupt's rights derived from a transaction with the Grant Company ("Grant"). This transaction involved either the conditional sale or lease of an aircraft to Grant by the bankrupt. An "aircraft lease," which the trustee maintains is a conditional sale contract, was executed. The bankrupt gave the bank a security interest in the lease/conditional sale contract by written assignment. The assignment was not recorded and is accordingly invalid against the trustee. To complete the collateral package, the bankrupt gave the bank a chattel mortgage which purported to give the bank a security interest in the underlying aircraft. The chattel mortgage was recorded. However, the chattel mortgage is subsequent to and subordinate to the "aircraft lease" between the bankrupt and Grant. If the Grant transaction is a conditional sale, the bankrupt's only interest in the aircraft was a security interest. Since the bank's security interest therein is conveyed by the assignment, the chattel mortgage

conveys nothing. If on the other hand, the Grant transaction involves a true lease, the chattel mortgage would cover only the lessor's reversion in the aircraft. Since all of the bank's rights were not perfected, the court below should have determined the nature and scope of the respective interests conveyed by the unrecorded assignment and the recorded chattel mortgage.

In granting summary judgment in favor of the bank, the district court did not rule on the trustee's theory of action, i.e., that the bank's security interest in Grant's post-petition payments was based solely on the unrecorded assignment of the lease/conditional sale contract and was unperfected and therefore invalid against the trustee. Instead, the court created a counterclaim by the bank for foreclosure of the chattel mortgage and gave the bank summary judgment on this unpleaded counterclaim. The expressed rationale of this ruling was that the chattel mortgage was the chief security instrument. The court ignored the existence of the Grant lease and treated the unrecorded assignment thereof as superfluous. Summary judgment on this "counterclaim" was improper because as a matter of law the chattel mortgage did not cover the lease payments and because the affirmative defenses of laches and waiver were available against the counterclaim raising triable issues of fact.

The Issues Presented

The issues to be determined on this appeal fall into three broad areas, two of which raise subsidiary issues. These issues are:

I. Whether an unrecorded assignment of aircraft "chattel paper" is invalid against the assignor's trustee in bankruptcy from the date of petition filing?

A. Whether a trustee in bankruptcy using his status under §70c of the Act, 11 U.S.C. §110c, is deemed to be without "actual notice"?

B. Whether the assignment of a true lease affects an interest in the leased property?

C. Whether a security interest covering specific goods subject to a lease grants a security interest in anything more than the lessor's reversion?

II. Whether the assigned "lease" is a conditional sale contract as defined at 49 U.S.C. §1301(16)?

III. Whether summary judgment was properly granted in favor of defendant on its unpledged counterclaim?

A. Whether the collateral description contained in the recorded chattel mortgage reasonably described the assigned "lease" as collateral covered by the mortgage?

B. Assuming the assigned "lease" is a conditional sale contract, whether the chattel mortgage covers any property interest owned by the bankrupt?

C. Whether the district court erred in considering the stipulation between the parties as evidence that the fund realized under the stipulation represented the bank's chattel mortgage interest?

D. Whether the existence of the affirmative defenses of "laches" and "waiver" in regard to defendant's unpledged counterclaim raises triable issues of fact, requiring denial of summary judgment on the counterclaim? ,

E. Assuming arguendo that summary judgment on the unpledged counterclaim was properly granted, whether the district court erred in dismissing the complaint where the relief requested therein, if granted, would have resulted in a substantial affirmative judgment in favor of plaintiff?

The Facts

A. The Grant Lease - A Conditional Sale Contract

On or about March 7, 1969 Grant paid a \$25,000.00 deposit to [✓] Jack Adams Aircraft Sales, Inc., ("Adams") for the purchase of a North American aircraft (A79, A89). Grant subsequently arranged for Leasing Consultants Incorporated ("Leasing") to finance this purchase. On or about April 11, 1969, a contract was executed between Leasing and Grant; and Leasing agreed (A79, A89) to purchase the aircraft from Adams.

The contract executed on April 11, 1969 included a document denominated an "aircraft lease" (A7-A8); an "aircraft schedule" (A11); an "option to purchase" (A12); and a "guaranty" (A10). Grant committed itself to pay Leasing \$1,113,000.00 in monthly installments of \$11,593.75 (A11, A73). The "option to purchase" permitted Grant to complete its purchase of the aircraft by paying an additional \$79,500.00 at the end of the 96 month term.

At the closing Grant gave Leasing its check for \$32,968.75 (A92), which together with the \$25,000.00 deposit paid by Grant to Adams, constituted prepayment of the first and last four installments (A11). Leasing subsequently honored Adam's \$800,000.00 draft (A90) drawn against Leasing and received a bill of sale (A91) which was recorded with the Administrator. The "aircraft lease" was not submitted for recordation at that time.

B. The Secured Loan from Defendant to Bankrupt.

On or about March 13, 1970, National Bank of North America ("National") made a \$500,000.00 loan to Leasing Consultants Incorporated ("Leasing"). (A22) Leasing executed and delivered to National three documents, i.e., a secured promissory note (A22-A26), a chattel mortgage (A27-A60) covering an aircraft, and an assignment (A13) of a lease between Leasing and the Grant Company ("Grant") which lease covered the aircraft described in the chattel mortgage. National subsequently received an agreement (A93) signed by Grant acknowledging the assignment and agreeing to it.

Since the perfection of security interests in aircraft and aircraft related transactions is governed by the Federal Aviation Act of 1958, National attempted to record both the chattel mortgage and the assignment of the lease/conditional sale contract with the Administrator of the Federal Aviation Administration ("Administrator"). (A95 - A100)

National experienced considerable difficulty in meeting the formal requirements for the filing of these instruments, and while the chattel mortgage was eventually filed, National inexplicably never managed to file the assignment. (A16, A74)

Under the terms of the unrecorded assignment, Grant paid \$11,593.75 per month to Leasing (A73). Payments were to continue for 96 months. Each payment was mailed to National and was deposited in a bank account maintained by Leasing at one of National's branches. On the 20th day of each month National would debit that account in the sum of \$11,122.50, the amount of the monthly loan installment.

C. Leasing's Bankruptcy

On August 18, 1970, Leasing filed a petition for arrangement under Chapter XI of the Bankruptcy Act in the United States District Court for the Eastern District of New York (A74). Leasing consented to adjudication on October 14, 1970 and an order

was entered on October 16, 1970 adjudicating Leasing a bankrupt and appointing George Feldman as trustee in bankruptcy (A74).

The bankrupt estate retained a large equity in the
*
Grant lease. On or about May 10, 1971, the trustee received an offer from Grant to purchase the aircraft free and clear of
National's purported lien for \$560,000.00 (A64, A67). When the offer was brought before the Bankruptcy Court, National resisted the sale. In any event, the offer was too low and the trustee recommended refusal. No sale was made at that time.

D. The Trustee Notifies National of His Claim

In January of 1973, the trustee's attorneys realized the significance of a secured party's failure to federally record the assignment of an aircraft conditional sale contract or aircraft lease in the context of a suit in the United States District Court in Florida. This realization led to the trustee's successful attacks against unrecorded assignments made by Leasing to Chase Manhattan Bank, N.A. ("Chase") and First
**
National City Bank ("CitiBank"), both on appeal to this court.

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The estate had a long term equity in the Grant lease of \$341,073.25 (A65).

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Reported at 368 F. Supp. 1327 and 368 F. Supp. 1333, respectively.

Counsel to the trustee immediately contacted counsel for National and between February of 1973 and January of 1974 had many discussions about the merits of the case and possible settlement (A110). National agreed to toll the statute of limitations during this period (A110). Suit was only commenced when the district court ruled on the Chase and CitiBank cases and there appeared to be no chance for settlement.

E. The Stipulation of November 12, 1973

In the course of these discussions Grant fell behind in its payments under the aircraft lease. The trustee and National both agreed to permit Grant to prepay its obligations. The "stipulation" (A109-A112) put into evidence at the June 28, 1974 hearing (hereinafter the "Stipulation") was an attempt to accomplish this purpose without disturbing the status quo. Grant had offered to purchase the aircraft by prepaying its obligations under the aircraft lease at a 12% discount and prepaying the purchase option at a 7.5% discount (A103). The purchase price was to be \$433,705.58 (A103, A104). When the sale was consummated, \$160,473.44, representing the balance due National under its loan to Leasing was placed at interest to be specially held by the trustee and the balance was given to the trustee to be deposited in the general funds of the estate. Both parties expressly reserved all rights.

F. Bringing Suit - The Complaint

Following Judge Bauman's decisions in the Chase and CitiBank cases a complaint (A3-A6) against National was prepared and filed. The complaint contained two causes of action. The first cause of action seeks recovery of \$440,562.50 in post-petition payments made by Grant under the assigned "aircraft lease" between August 16, 1970 and November 12, 1973. The second cause of action seeks a determination that the \$160,473.44 fund created by the stipulation belongs to the bankrupt estate.

G. Defendant's Motion to Dismiss

On March 18, 1974 National made a motion (A14) to dismiss the complaint "on the grounds that the complaint fails to state a claim upon which relief can be granted; the claim asserted in the complaint is barred by the Statute of Limitations and the plaintiff lacks the capacity to sue..." Annexed to the motion was a Rule 9(g) statement (A15-A16) and an attorney's affidavit with exhibits (A17-A68). The gravamen of the motion was that National could retain the monies under its recorded chattel mortgage, and that in any event, the suit was barred by the two year limitation period contained in the Bankruptcy Act §11e and a trustee in bankruptcy could not benefit from the strictures of

49 U.S.C. §1403(c). Further contentions were made in an accompanying memorandum of law.

H. Plaintiff's Cross-Motion for Summary Judgment.

On April 16, 1974, the trustee made a cross-motion for summary judgment (A69-A71). This motion was supported by a Rule 9(g) statement (A72-A75), a response to National's Rule 9(g) statement (A75-A77), and an attorney's affidavit with exhibits (A78-A106). The trustee's position was that the assignment was invalid for want of federal recordation; that the chattel mortgage did not give National a security interest in Grant's monetary obligations to Leasing; that the lease was really a conditional sale contract so that Leasing did not own the aircraft at the time the chattel mortgage was executed; that if the lease were a true lease, the chattel mortgage covered only the lessor's reversion; that a six-year statute of limitations borrowed from the law of New York governed; and that the trustee had standing to maintain the suit.

National responded to the trustee's Rule 9(g) statement (A107-A108). Additional memoranda were served and filed by both National and the trustee.

I. The Court's Oral Decision and Response to Requests for Additional Findings

Oral argument was heard before District Judge Jack B. Weinstein on June 28, 1974 and the court granted summary judgment in favor of National (A122 at 1. 16). The court concluded:

"...the documents in the case require that the cash assets of the sale of the plane be treated as if the cash were the plane and that this action, insofar as it involves a counterclaim by National Bank, be treated as if it were a foreclosure action against the plane, i.e., the cash." (A121 at 11. 19-25.)

"Upon foreclosure the bank would have been entitled to the plane and is, therefore, entitled to so much of the cash as is owed to it under the chattel mortgage." (A122 at 11. 1-5).

That summary judgment was being allowed on an unpleaded counter-claim sounding in foreclosure was reiterated in response to requests for specific additional findings made by the trustee's counsel.

"...[the] chattel mortgage is the primary instrument and that has been properly filed, and it is the chattel mortgage that we are now in effect foreclosing." (A127 at 11. 22-25.)

"...[the Trustee's] claim is that the bank was not entitled to anything, so far as the plane was concerned, and could not foreclose against the plane itself....They did not foreclose because [the trustee] and the bank agreed to sell the asset immediately on good terms, without foreclosing, which would have caused an extensive delay and would have made it possible... for the asset to have wasted....that is the way I read the documents...." (A134 at 11. 8-10, 14-18, 20-21, 24-25.)

The court found that:

"There was no question that the cash was to stand in place of the plane." (A136 at 11. 5-6.)

It is assumed that the court's repeated reference to the "cash" refers to the proceeds derived under the Stipulation. These proceeds amount to \$433,705.58 (A148). [Pursuant to the Stipulation, the bankruptcy estate received \$273,232.14 and the \$160,473.44 balance is being held specially subject to the court's determination.] Judgment on the unpledged counterclaim would have given National the \$160,473.44 and a \$273,232.14 offset against the claim contained in the trustee's first cause of action which seeks recovery of \$440,562.50 in post-petition payments. If the law entitles the trustee to a \$440,562.50 judgment as demanded in the complaint, the trustee should have been granted judgment in the sum of \$167,330.36 plus interest. But the court ignored plaintiff's first cause of action and the motion for reargument was denied (A155), throwing the court's stated rationale in doubt.

The court made other findings that are either unsupported in the record or contrary to the prevailing law, and in addition, refused to make several crucial determinations. Thus the court erroneously found that the trustee had "actual notice" of the assignment (A124 at 1. 25.), stating:

"I think the whole handling of this claim over this long period suggests that [the trustee] had notice.

"The court takes judicial notice of the fact that the trustee and his counsel's extremely competent handling of these litigations suggests that they would have made a full investigation." (A140 at l. 24-A141 at l. 7.)

The court found "...there was sufficient filing of notice..." (A123 at ll. 9-10.), "...that any reasonable creditor would have been advised by the filing of the chattel mortgage of the lease and of its filing in New York...." (A125 at ll. 16-19), "...that anybody...would have been on notice through the chattel mortgage of everything that he had to know and could easily have traced the matter...." (A130 at ll. 9-13.) The court failed to limit its actual notice determination to the date the bankruptcy petition was filed and also ignored the many cases in this circuit holding that a §70c trustee is deemed to be without "actual notice."

The court also assumed without justification that the Grant lease was a true lease as opposed to a conditional sale contract.

"The Court: ...This was not a conditional sale, It was a lease..."

"Mr. Zimmerman: Your Honor, does your Honor make a finding of fact that this was not a conditional sale?"

"The Court: That is right...." (A130 at ll. 15-20)

In so finding the court failed to apply the documentary evidence to the Congressional definition of "conditional sale" contained in the Federal Aviation Act. See 49 U.S.C. §1301(16).

The court also interpreted the stipulation to mean "...that the trustee intended that the cash stand in place of the plane." (A133 at 11. 15-21.) But the form of offer outlined in the Stipulation expresses a contrary intention.

"10. Grant has offered to purchase the [airplane] by prepaying its obligations under the aircraft lease at a 12% discount and prepaying the purchase option at a 7.5% discount...." (A110)

It was National who wanted the cash to "stand in place of the plane," not the trustee. Thus the Stipulation provides:

"...Bank [specifically] reserves the right to...
(2) Contend that the entire proceeds of the sale of the Saber Liner to Grant, including the portion of the purchase price received by the Trustee, is subject to Bank's chattel mortgage...."
(A112)

The district court lost sight of the fact that the Stipulation was executed in the midst of this legal controversy. It therefore provided:

"D. This stipulation shall be totally without prejudice to the respective rights of Bank and the Trustee and no statements as to the facts or issues heretofore set forth shall be binding or admissible in evidence in any legal proceeding between the parties hereto." (A111-A112)

Thus the Stipulation should never have gone into evidence and the court's conclusions drawn from its terms were unwarranted.

The court refused to determine whether "the description contained in the chattel mortgage covers, as collateral, the Grant lease and/or the proceeds of the Grant lease." (A132 at 11. 22-25.), responding:

"I make no such finding. I do not think it necessary." (A133 at 11. 2-3.)

The court refused to determine the validity of the assignment, although that issue goes to the very heart of the trustee's two causes of action.

"It is not necessary to determine on this motion whether the federal statute requires the assignment to be filed with the FAA.... nothing really turns on the question of the assignment of the lease..." (A123 at 11. 5-11.)

When the trustee's counsel asked for a finding that the assignment of the lease was invalid against the trustee, the very issue that underlies the complaint (A128 at 11. 1-5), the court responded:

"All the information I have indicates that the assignment was a valid assignment." (A128 at 1. 25 - A129 at 1. 3.)

But, when considered in the light of the federal recording statute, the court added:

"I haven't got sufficient information. If you are now contesting it, you haven't contested it up to this point." (A129 at 11. 9-11.)

When the trustee's counsel pointed out that the entire complaint rested on the assertion that the assignment of the lease was invalid because unrecorded (A129 at 11. 12-13), the court backed off:

"And I haven't determined [it], because it is not necessary to my decision, whether the federal statutes require that it be recorded." (A130 at 11. 5-8).

In view of the court's granting summary judgment to defendant on its unpledged counterclaim, such a determination was obviously crucial.

Point I

THE UNRECORDED ASSIGNMENT OF AN
AIRCRAFT CONDITIONAL SALE CONTRACT
IS INVALID AGAINST THE ASSIGNOR'S TRUSTEE*

Congress has required recordation with the Administrator of all "conveyances" affecting title or other interests in aircraft. Federal Aviation Act §503(a)(1), 49 U.S.C. §1403 (a)(1). The Administrator's regulations state that the assignment of a vendor's interest under a conditional sale contract is a recordable conveyance. 14 C.F.R. §§49.17(d)(2) and 49.31(a). Recordable conveyances which are not filed for recordation with The Administrator are invalid against third persons without "actual notice" of the conveyance. Federal Aviation Act §503(c), 49 U.S.C. §1403(c).

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* This issue has been briefed extensively on Citibank's appeal from District Judge Bauman's decision in Feldman v. First National City Bank, supra, docket number 74-1893, which case is scheduled for argument the week of November 18, 1974. A repetition of the trustee's extensive argument would serve no useful function at this juncture, so the trustee will limit himself to a summary of the argument with appropriate references to the record in this case and responses to certain arguments raised by National before the district court.

Since the Grant lease is a conditional sale contract, see infra, at 31, and since Leasing's assignment of the Grant lease to National was admittedly not filed for recordation with the Administrator, the assignment is invalid against third persons without "actual notice" of the assignment. Leasing's trustee in bankruptcy is such a person.

As previously noted, the District Court found that the trustee had actual notice of the assignment. (p. 12, l. 25.) Not only is that finding contrary to the prevailing law, but the District Court improperly considered the trustee's post-bankruptcy investigation in finding "actual notice" (p. 28 at 11. 24-25, p. 29 at 11. 1-7). Lewis v. Manufacturers National Bank of Detroit, 364 U.S. 603 (1961). [Where the Supreme Court expressly ruled that the trustee's §70c rights are determined as of the date of petition filing.] The district court also confused "constructive notice" with "actual notice" inferring that the federally recorded chattel

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"Actual notice differs from constructive notice in that the latter is a legal inference from established facts, while actual notice may be actual knowledge or notice implied from the facts." The Tompkins, 13 F.2d, 552, 554 (2d Cir. 1926). "Constructive notice is generally held to be that notice which a person is deemed to have by operation of law, commonly through the recording statutes." Sands v. United States, 198 F. Supp. 880, 884 (W. D. Wash. 1960). At best recorded instruments such as the chattel mortgage would constitute constructive notice of the assignment unless actually reviewed.

mortgage (p. 18 at 11. 9-13) and National's filing of U.C.C. financing statements in Albany and in Queens county (p. 13 at 11. 16-19) gave the trustee actual notice of the assignment.

*

This court, on numerous occasions has held that under §70c of the Bankruptcy Act, 11 U.S.C. §110c, the trustee is a hypothetical lien creditor without actual notice. Fifth Third Union Trust Co. v. Kennedy, 185 F.2d 833, 835 (2d Cir. 1950); Hoffman v. Cream-O-Products, 180 F.2d 649, 650 (2d Cir. 1950), cert. den. 340 U.S. 815 (1950); Empire State Chair Co. v. Beldock, 140 F.2d 587 (2d Cir. 1944), cert. den. 322 U.S. 760 (1944); White v. Steinman, 120 F.2d 799, 802 (2d Cir. 1941), cert. den. 314 U.S. 659 (1941). See 4A Collier on Bankruptcy, ¶70.53, n. 10 (14th ed. 1973). In the Kennedy case, supra, the §70c trustee of a conditional vendee successfully invalidated the vendor's security title because

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National's filing of U.C.C. financing statements, if relevant, was inadequate because Leasing's only place of business in New York State was in Nassau County as opposed to Queens Count. See U.C.C. §9-401(c).

the contract had not been filed within thirty days after delivery of the property to the vendee as required by Vermont law. This court stated:

"The remaining question is whether this appellee does have the standing of an attaching creditor with the meaning of §2775, V.S. The rule in Vermont is that an attaching creditor, who would avoid a vendor's lien because the contract was not recorded as the above statute requires, has the burden of showing that the attachment was made without knowledge of the existence of the vendor's lien. Singer Mfg. Co. v. Nash, 70 Vt. 434, 41 A. 429.

"This appellee, however, is not actually an attaching creditor but a hypothetical one. He has that status by virtue of §70, sub. c, of the Bankruptcy Act, 11 U.S.C.A. §110, sub. c. And it is federal law which controls in this respect. Commercial Credit Co., Inc. v. Davidson, 5 Cir. 112 F.2d 54. He has, moreover, not only the status of an attaching creditor but that of one without notice of an unrecorded prior lien. Tapling v. Northwestern Nat. Bank, 3 Cir., 101 F.274; Cooper Grocery Co. v. Park, 5 Cir. 218 F.42; Industrial Finance Corp. v. Cappleman, 4 Cir., 284 F.8; Collier on Bankruptcy 14 Ed. §§70.53, 70.49. As this advantage comes to him by virtue of the Act, he starts in the same position to defeat an unrecorded vendor's lien that an attaching creditor in Vermont attains by discharging his burden to prove his lack of notice of the lien. Whether any creditor of the bankrupt did have notice is irrelevant. Hoffman v. Cream-O-Products, 2 Cir., 180 F.2d 649." Id., 185 F.2d at 835.

In the Kennedy case, supra, an actual examination of the record would have revealed the belatedly filed contract. In White v. Steinman, supra, an actual examination would have

revealed the prematurely filed contract. Similarly, in Empire State Chair Co. v. Beldock, supra, and Hoffman v. Cream-O-Products, supra, an actual examination of the record would have found the contract which the court voided because the description of the goods was omitted in one instance and because the terms of payment were omitted in the latter case. An actual examination would have put the examiner on notice of inquiry provoking facts. Since this Court did not charge the trustees in any of these cases with the knowledge that would have been acquired by a search of the record, there is no basis for charging the plaintiff-trustee with such knowledge at bar.

Since plaintiff-trustee is a third person without "actual notice" of the assignment of the conditional sale contract, the assignment is invalid against him from the date of petition filing forward. It follows that the post-petition payments made by Grant to National under the assignment belong to the trustee. It is undisputed that Grant made 38 payments of \$11,575.50, totalling \$440,562.50 to National between August 18, 1970 and November 12, 1973.

(A74, A108) Thus the trustee is entitled to judgment on his first cause of action in that sum, with interest on the individual payments from their respective dates of receipt.

Whether the trustee is entitled to judgment on his second cause of action depends on whether the cash derived under the stipulation represents payments under the assigned lease or the fair market value of the aircraft, an issue discussed below, at 29.

Point II

THE UNRECORDED ASSIGNMENT
OF AN AIRCRAFT LEASE IS
INVALID AGAINST THE
ASSIGNOR'S TRUSTEE *

Assuming arguendo that the Grant lease is a true lease, Leasing's assignment of it to National is invalid because unrecorded. Congress has required recordation with the Administrator of all "conveyances" affecting title to or other interests in aircraft, Federal Aviation Act §503(a)(1), 49 U.S.C. §1403(a)(1), and has declared recordable conveyances which are not filed for recordation invalid against third persons without "actual notice" of the conveyance. Federal Aviation Act §503(c), 49 U.S.C. §1403(c). The trustee under §70c of the Bankruptcy Act, 11 U.S.C. §110c is such a third person without actual notice as can invalidate such an unrecorded conveyance. See point I, supra, at 31.

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* This issue has been briefed extensively by the trustee in answering and sur-reply briefs on Chase's appeal from District Judge Bauman's decision in Feldman v. Chase Manhattan Bank, N.A., supra, docket number 74-1277, which case is scheduled for argument the week of November 18, 1974. A repetition of the trustee's extensive argument would serve no useful function at this juncture, so the trustee will limit himself to a summary of the argument with appropriate references to the record in this case and responses to arguments raised by National before the district court.

The legal issue to be resolved is whether the "assignment" of a true lease is a conveyance subject to recordation with the Administrator as determined by District Judge Bauman in Feldman v. Chase Manhattan Bank, N.A., supra. Congress has defined the term "conveyance" to include any "...instrument affecting title to, or interest in, property." Federal Aviation Act §101(17), 49 U.S.C. §1301(17). The Administrator's regulations paraphrase the statutory definition stating that a recordable conveyance includes any "...instrument affecting title to, or any interest in, aircraft." 14 C.F.R. §49.31(a). In this context Judge Bauman stated:

"It would seem invontrovertible that the statutory language "conveyance which affects ... any interest in" an airplane should encompass an assignment of a lease. Clearly the present possessory right and the entitlement to rentals conferred by a lease agreement are property "interests" as the term has been generally understood; less than "title" perhaps, but "interests" nonetheless. It then follows that assigning a lease "affects" the lessor's interest by transferring its primary incident, the right to receive rentals." Id., 368 F. Supp. at 1332.

Judge Bauman's analysis is backed up by a review of the treatment of security interests in chattel paper under the Uniform Commercial Code ("Code.") The Grant lease is chattel

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paper under the Code definition , U.C.C. §9-105(b), whether it is a true lease or a conditional sale contract (or even a chattel mortgage.) See Official Comment to U.C.C. §9-308, 63 1/2 McKinney's U.C.C., at 500 (1974). Security interests in chattel paper are normally created by assignment and there are specific provisions under the federal act and regulations stating that assignments of mortgages and interests under conditional sale contracts are recordable conveyances. Federal Aviation Act §101(17), 49 U.S.C. §1301(17), 14 C.F.R. §49.31(a), and specific provisions governing the filing requirements, 14 C.F.R. §49.17(d)(2) and 49.17(e)(3). Uniformity requires that assignments of lease/chattel paper also be recorded particularly because of the difficulty in ascertaining whether a lease is a disguised security agreement. See In re Leasing Consultants, Incorporated, 486 F.2d 367 (2d 1973). National acknowledged the need to record the assignment by making three unsuccessful attempts to file it for recordation (A97, A99, A100).

Since the assignment of a true lease is a recordable conveyance it is invalid against the assignor's trustee in

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U.C.C. §9-105(b) defines "chattel paper" as "...a writing ...which evidences both a monetary obligation and a security interest in or a lease of specific goods..."

bankruptcy from the date the bankruptcy petition was filed because it was not recorded. It follows that the post-bankruptcy payments made by Grant to National under the assigned lease belong to the trustee. It is undisputed that Grant made 38 payments of \$11,575.50 totalling \$440,562.50 to National between August 18, 1970 and November 12, 1973. Thus the trustee is entitled to judgment on his first cause of action in that sum, with interest on the individual payments from their respective dates of receipt.

The fate of the trustee's second cause of action depends upon other considerations. In In re Leasing Consultants, Incorporated, supra, this court concluded that a lessor can grant separate security interests in the lease (which is chattel paper) and in the lessor's reversion (which is goods), and that these separate security interests were subject to different perfection requirements. Applying the same analysis to the facts at bar, it is reasonable to conclude that the unrecorded assignment (A 13) grants a

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security interest in the lease/chattel paper (A7-A12) and the recorded chattel mortgage grants a security interest
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in the lessor's reversion.

The value of the lessor's reversion must be determined before judgment can be granted on the trustee's second cause of action. The trustee submits that the value of that reversion, if a reversion exists, is the amount of the purchase option, i.e. \$79,500.00 payable in April of 1976, discounted

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The assignment states: "Leasing...by this instrument does sell, assign, transfer and set over, unto National ... all the right, title and interest of the Assignor [Leasing] under, in and to that certain Lease Agreement, Lease No. 1293, dated as of April 11, 1969, between the Assignor, as lessor, and Grant Company...as lessee...including without limitation, all rental payments and other monies...due and to become due to the Assignor under, and all claims for damages arising out of the breach of, the Lease, and the right of the Assignor to terminate the Lease, to perform thereunder and to compel performance of the terms thereof..."

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The chattel mortgage contains the following collateral descriptions: "...all of the property described in Schedule I hereto attached, together with all appliances, instruments, radios, navigation aids, equipment and accessories, all additions which may from time to time be installed in or be appurtenant thereto, all substitutions or replacements therefor, and all sales warranties and/or obligations to supply spare parts in respect thereof (herein called the "Mortgaged property") . . ."

Schedule I describes the collateral as follows: "One (1) Saberliner Executive Jet Aircraft, 1965, Model 265-40, Mfg. Serial No. 282-38, F.A.A. Reg. No. N299LR [and] Pratt & Whitney Engines Numbers JT12A-6A."

to November 12, 1973. Under the terms of Grant's offer (A103 - A104) that amount would be \$60,815.42 and the trustee would be entitled to judgment on his second cause of action in the sum of \$99,658.02 plus interest.

Point III

THE GRANT LEASE IS A
CONDITIONAL SALE CONTRACT

The Federal Aviation Act of 1958 contains its own definition of "conditional sale" which is clearly applicable to the recording provisions contained in that statute. Western Union Telegraph Co. v. Lenroot, 323 U.S. 490 (1945); Porter v. Bledsoe, 159 F.2d 495 (4th Cir. 1947). Federal Aviation Act of 1958, Section 101(16), 49 U.S.C. §1301(16) provides:

"As used in this chapter, unless the context otherwise requires ---

" 'Conditional sale means... (b) any contract for ... the leasing of an aircraft ... by which the ... lessee contracts to pay as compensation a sum substantially equivalent to the value thereof, and by which it is agreed that the ... lessee ... had the option of becoming the owner thereof upon full compliance with the terms of the contract.'"

Thus aircraft leases are conditional sale contracts when the lessee has an option to become the airplane's owner upon fulfillment of its contractual obligations and when its lease obligations are substantially equivalent to the aircraft's value. The Grant lease contained a purchase option (A12) which was exercizable upon completion of Grant's

other lease obligations. And Grant's contractual obligation to pay \$1,113,000.00 in lease rentals over an eight year period and the \$79,500.00 option price at the end of the eight years is clearly equivalent to the \$825,000.00 aircraft purchase price plus interest for the eight year period. Thus the Grant lease meets the statutory test for a conditional sale contract.

When this issue was briefed before the District Court, Nationals' response to this proposition was to attack the validity of Grant's option as against National. But the validity of Grant's option is not at issue. What is at issue is the proper characterization of the Grant lease as of the date it was executed. In re Sherwood Diversified Services, Inc., 73 B. 213, S.D.N.Y. October 4, 1974, Opinion of Henry F. Werker at 10

No other determination is plausible since the nature of the contract, i.e. lease or conditional sale, has quasi-criminal repercussions. It is unlawful for an aircraft to be registered other than in the name of its "owner", Federal

Aviation Act, §501(a), 49 U.S.C. §1401(a), and while under a true lease the lessor is the owner, under a lease/conditional sale contract, the lessee is the owner. 14 C.F.R. § 47.5(c), In re Boone, 1 C.A.A. 671, 673 (1941).

Point IV

SUMMARY JUDGMENT SHOULD HAVE NOT BEEN
GRANTED ON AN UNPLEADED COUNTERCLAIM
WHICH RAISED ISSUES OF FACT AND LAW

The District Court granted summary judgment in favor of National on a counterclaim based on foreclosure of National's chattel mortgage (A123 at 11. 19-25.) Since National elected to move against the trustee's complaint rather than answer it, no pleading setting forth National's counterclaim was served and filed as contemplated by Rule 13 of the Federal Rules of Civil Procedure. Under these circumstances, the trustee was not directly confronted with a claim for affirmative relief, had no opportunity to specifically deny the averments making up the counterclaim, and had no opportunity to plead affirmative defenses in response to the counterclaim. See Rules 8(a), (b) and (c) of the Federal Rules of Civil Procedure.

A. The District Court Erred in Refusing to Determine Whether the Collateral Description Contained in the Chattel Mortgage Reasonably Described the Grant Lease as Collateral.

There is a substantial legal issue regarding the nature of the property covered by the chattel mortgage. Such property is limited to the collateral description contained in the schedule annexed to the chattel mortgage (A60). Mammoth Storage Warehouse v. Woodhouse, 136 N.Y.S.2d 594 (Sup. Ct. 1955). At bar,

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the schedule describes only a certain airplane. The schedule does not describe the Grant lease as collateral covered by the chattel mortgage. In In re Laminated Veneers Co., Inc., 471 F.2d 1124, 1125 (2d Cir. 1973), this court held that if the collateral description contained in a security agreement does not reasonably identify the property, that security instrument does not create a security interest in that property. At bar it is the trustee's position that the collateral description contained in the chattel mortgage, as a matter of law, does not reasonably identify the Grant lease and/or Grant's monetary obligations under said lease as property covered by that security instrument. If the lease is a conditional sale contract, it covers nothing, conveys nothing and is therefore superfluous. All the collateral was covered by the unrecorded assignment. Alternatively, if the lease is a true lease, the mortgage description covers only Leasing's reversionary interest in the airplane, while the unrecorded assignment covers the lease rentals. Contrary to this court's holding in the Laminated Veneers case, supra, the district court found it unnecessary to consider this crucial issue (A132 at 1. 22 - A133 at 1. 3.)

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The chattel mortgage contains collateral description set forth supra, at 29.

This is surprising because the same court's decision in In re Leasing Consultants, Incorporated, 351 F. Supp. 1390 (E.D.N.Y. 1972), aff'd 486 F.2d 367 (2d Cir. 1973) drew a trenchant distinction between lease/chattel paper and a lessor's reversion as different kinds of collateral. As stated by District Judge Weinstein in that case:

"....By....assigning to the creditor all of its 'rights, title and interest in, to and under' the leases and the equipment, the lessor gave to the creditor a security interest in both the right to receive rental payments under the lease and in the reversionary interest in the underlying equipment." 351 F.Supp. at 1393.

"The distinction between the rights represented by the lease and those represented by the reversionary interest in the equipment is a real one, supported by logic and precedent...." 351 F.Supp. at 1394.

Applying the same distinction to the case at bar, and assuming arguendo that the lease is a true lease as contended by National, it is obvious that the recorded chattel mortgage gave National a security interest in the lessor's reversion, while the unrecorded instrument, i.e., the assignment, created the security interest in the right to receive rental payments under the lease. Thus upon foreclosure under the chattel mortgage, National could only obtain the lessor's reversionary interest

* whatever its value. Only by foreclosing on the "assignment" could National be entitled to the Grant lease payments.

B. If the Grant Lease is a Conditional Sale Contract, There is no Lessor's Reversion, and the Chattel Mortgage is a Nullity.

The issue of whether the Grant lease is a conditional sale contract, briefed supra, at 31, is another issue which the district court handled perfunctorily. (A130 at 1. 15 - A132 at 1. 3.) A lease/conditional sale of an airplane is deemed made by the lessee/vendee. Federal Aviation Act §101(16), 49 U.S.C. §1301(16). The lessee/vendee, in this case Grant, becomes the "owner" of the aircraft. 14 C.F.R. §47.5(c), In re Boone, 1 C.A.A. 671, 673 (1941). Leasing, as lessor/vendor, had only a security interest in the airplane and nothing more. James Talcott, Inc. v. Franklin National Bank of Minneapolis, Minn. ___, 194 N.E.2d 775, 10 U.C.C. Rep. Serv. 11, 20 (1972).

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* The value of the lessor's reversion, if one exists, is discussed above at 29.

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The statutory definition of "conditional sale" concludes: "...The...lessee shall be deemed to be the person by whom such contract is made or given." 49 U.S.C. §1301(16).

The purported security interest in the aircraft granted by Leasing to National never attached, U.C.C. §9-204(1), because at the time Leasing executed the chattel mortgage, Leasing no longer owned the airplane. Main Investment Co. v. Gisolfi, 203 Pa. Super. 244, 199 A.2d 535, 2 U.C.C. Rep. Serv. 147, 150 (1964).

What confronts this court is the typical case of a secured party who failed to perfect its security interests. In this case, the collateral subject to National's security interest happens to be a conditional sale contract covering an aircraft, and not the aircraft itself. As noted by Professor Homer Kripke in McKinney's Practice Commentary to U.C.C. §9-302:

"In the typical case of a debt secured by a conditional sales contract...covering equipment: (1) the debt itself and its security together constitute chattel paper...The assignment of the debt must be perfected by the rules relating to the assignment of chattel paper..." 62 1/2 Mc Kinney's Cons. Laws. at 455 (1973).

Precisely the same situation is found at bar. A conditional sale contract covering an aircraft was the security for National's loan to Leasing, but National did not follow the rules for perfecting the assignment of a conditional sale contract. This failure was not due to ignorance, but due to laxness. National recognized the need to record the assignment, but failed to follow through (A82-A83). Since the chattel mortgage could not give

National a security interest in property previously transferred by Leasing, foreclosure under that instrument is futile.

C. The District Court Committed Reversible Error in Ruling that the Fund Realized under the Stipulation Represented National's Chattel Mortgage Interest.

The district court found that the fund created under the stipulation stood in place of the airplane and was subject to National's chattel mortgage. (A136 at 11. 5-6, A121 at 1. 19 - A122 at 1.5.) The finding was unsupported by the documentary evidence before the court, which the court expressly relied upon. (A121 at 11. 15-17, A123 at 11. 17-21.) At page 11 of its opinion (A123) the court stated that "...the stipulation dated November 12, 1973, marked as Defendant's Exhibit A, indicate[s] that reasonably construed the documents in the case require that the cash assets of the sale of the plane be treated as if the cash were the plane..."

The stipulation (A109-112) leads to no such conclusion. One of the obvious aims of the Stipulation was to leave open the question of what the "cash" represented. The Stipulation took no position on that issue and was intended to take no position. The trustee wanted the cash to represent payments under the as-

signed lease, as set forth in paragraph 10 of the Stipulation and in the offer itself (A103). National contended otherwise.

"...Bank does not agree that said sale represents a prepayment of Grant's obligation under the aircraft lease and purported purchase option." (A110)

The stipulation was not to affect the respective rights of the trustee and National and accordingly recited that it was inadmissible in evidence in any legal proceeding between the parties.

"D. This stipulation shall be totally without prejudice to the respective rights of Bank and the Trustee and no statements as to the facts or issues heretofore set forth shall be binding or admissible in evidence in any legal proceeding between the parties hereto. It is the intention of the Bank and Trustee that their respective rights, claims and defenses are not to be affected by the sale of the Saber Liner to Grant." (A111-A112).

It is thus obvious that the parties intended that no weight be placed on the stipulation in determining the merits of the case. A proper characterization of the fund realized under the stipulation must therefore be based on other considerations.

Under the aircraft lease (A7-A8) and aircraft schedule (A11) Grant had a contractual obligation to make thirty-nine (39) additional monthly payments of \$11,593.75 each. This was Grant's
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"10. Grant has offered to purchase the Saber Liner by prepaying its obligations under the aircraft lease at a 12% discount and prepaying the purchase option at a 7.5% discount. The tentative purchase price is \$433,705.58." (A110).

chattel paper obligation. See U.C.C. §9-105(b). This contractual/chattel paper obligation had a considerable value. Considering this value, Grant's written offer (A103) to purchase the airplane by paying the remaining installments and the purchase option price (A12) discounted to present value, is strong and convincing evidence that the fund represents Grant's discounted chattel paper obligations. The stipulation does not affect the weight of this evidence at all. It cannot be used as evidence of whether the fund represents a prepayment of Grant's chattel paper obligations and it cannot be used as evidence that the fund represents a foreclosure under the chattel mortgage.

National insisted that the stipulation contain specific reservations so that National could

"(2) Contend that the entire proceeds of the sale of the Saber Liner to Grant, including the portion of the purchase price received by the Trustee, is subject to Bank's chattel mortgage;

"(3) Contest any characterization of the proceeds of the sale of the aircraft agreed upon by Grant and the Trustee;

"(4) Contend that the Bank has a right to the fair market value of the Saber Liner as of the terminal date of the lease; and

"(5) Establish an offset against any claim by the Trustee against Bank." (A112)

The right to make a contention however, does not relieve the contending party of its burden of supporting its contentions with clear and

convincing evidence. State Farm Mut. Auto. Ins. Co. v. Koval, 146 F.2d 118, 120 (10th Cir. 1944); National Lead Co. v. Nulsen, 131 F.2d 51, 56 (8th Cir. 1942), cert. den. 318 U.S. 758 (1943). National submitted no evidence other than the promissory note (A22 - A26) and the chattel mortgage (A27 - A60) and neither of these documents is dispositive on the issue. The affidavit of National's attorney, which avers that Grant's offer was in a sum approximating the plane's market value (A19) is entitled to no weight because Mr. D'Auria's qualifications as an expert witness on aircraft values were not set forth. In any event, Mr. D'Auria's unwarranted conclusion is offset by the trustee's notation in his motion for reargument that Grant had immediately resold the aircraft for \$560,000.00 (A150) substantially more than the \$433,000.00 fund realized under the stipulation.

The only documentary evidence submitted on this issue, i.e., Grant's offer (A103), stands uncontradicted in the record, and supported by common sense which requires that considerable value be assigned to a contractual obligation to pay \$457,156.25 over thirty-nine (39) months and an additional \$79,500.00 after forty-three (43) months. (A104). This alone requires a reversal of the district court's judgment.

D. Summary Judgment on National's Unpledged Counterclaim was Improper Because There are Material Issues of Fact in Dispute Regarding that Counterclaim.

Summary judgment is improper where there are material factual issues in dispute. United States v. Diebold, Inc., 369 U.S. 654 (1962); Empire Electronics Co., Inc. v. United States, 311 F.2d 175 (2d Cir. 1962); Arnstein v. Porter, 154 F.2d 464, 471 (2d Cir. 1946).

It must be assumed that National's counterclaim, had it been made in a pleading, would have alleged: (1) the existence of its chattel mortgage; (2) the amount of Leasing's indebtedness to National; (3) the failure of Leasing to pay this indebtedness or some other default; and (4) the property in regard to which National was foreclosing. 13 Carmody Wait 2d, §84:173, at 290-291 (1966).

The only defaults mentioned by National were Leasing's filing of a petition for arrangement on August 18, 1970 and Leasing's subsequent adjudication as a bankrupt on October 16, 1970. See Section 4.1 of the chattel mortgage (A44-A47). The lengthy hiatus between 1970 and 1974 indicates that National waived the event of default, or in any event, that National is guilty of laches in seeking to foreclose more than three

years after the alleged event of default. These defenses find support in National's opposition to the trustee's 1971 motion to sell the airplane free and clear of National's security interests (A 62-A 66) and by National's failure to seek foreclosure following receipt of notification of the trustee's claim against the assigned lease payments early in 1973.

While the foregoing allegations have only minimal support in the record below, this is because the trustee's papers were not responding to a motion for summary judgment addressed to the unpledged counterclaim. Certainly the affirmative defenses of waiver and laches require trial. Baker v. Nason, 236 F.2d 482, 493 (5th Cir. 1956).

Point V

ASSUMING ARGUENDO THAT SUMMARY JUDGMENT
ON THE UNPLEADED COUNTERCLAIM WAS WARRANTED,
THE TRUSTEE WAS ENTITLED TO AN
AFFIRMATIVE JUDGMENT IN EXCESS OF \$167,000.

On motion for reargument (A147) the trustee advised the district court that treating the stipulation as a foreclosure and granting National summary judgment on a counterclaim sounding in foreclosure did not dispose of the whole case. The district court disregarded this argument denying the motion (A155).

But the motion had obvious merit. The sale pursuant to stipulation realized \$433,705.58 (A103, A104, A148.) Pursuant to the terms of the stipulation (A111), \$160,473.44 was used to purchase a certificate of deposit which was to be held specially by the trustee. The balance in the sum of \$273,232.14 was deposited by the trustee in the general funds of the bankrupt estate. Treating the stipulation as a foreclosure, summary judgment on a foreclosure counterclaim would be in the total sum of \$433,705.58.

In terms of the two causes of action contained in the complaint, summary judgment on the trustee's second cause of action would be granted in favor of National, giving National the \$160,473.44 certificate of deposit; and National would have an additional \$273,232.14 judgment available as a set-off against the trustee's first cause of action which sought recovery of \$440,562.50 plus interest. A determination in favor of the trustee on his first cause of action (see points I and II, infra) would have given the trustee an affirmative judgment in excess of \$167,000.00 against National. It was thus reversible error for the district court not to consider the issues raised by the trustee's first cause of action.

CONCLUSION

FOR THE FOREGOING REASONS, THE JUDGMENT BELOW
SHOULD BE REVERSED.

Respectfully submitted,

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George A. Hahn,
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Of Counsel.

US COURT OF APPEALS: SECOND CIRCUIT
Index No.FELDMAN,
Plaintiff-Appellant,

against

Affidavit of Personal Service

NAT'L BANK OF NOR. AMER.,
Defendant-Appellee.

STATE OF NEW YORK, COUNTY OF NEW YORK ss.:

I, James Steele, being duly sworn,
 deposes and says that deponent is not a party to the action, is over 18 years of age and resides at
 250 West 146th Street, New York, New York
 That on the 28 29 day of October 1974 at 40 Wall St., New York
 deponent served the annexed Brief upon

Cole & Deitz

the in this action by delivering a true copy thereof to said individual
 personally. Deponent knew the person so served to be the person mentioned and described in said
 papers as the Attorney(s) herein,

Sworn to before me, this 29
 day of October 1974

James Steele
Print name beneath signature

JAMES STEELE

Robert T. Brin

ROBERT T. BRIN
 NOTARY PUBLIC, STATE OF NEW YORK
 NO. 31-35700
 QUALIFIED IN NEW YORK COUNTY
 COMMISSION EXPIRED MARCH 30, 1975

